NOS. 82-818 and 82-852

Office-Supreme Court, U.S.
FILED
MAY 9 1983
ALEXANDER L. STEVAS,
CLERK

Supreme Court of the United States

OCTOBER TERM, 1982

NATIONAL LABOR RELATIONS BOARD, PETITIONER (82-818)

v.

BILDISCO AND BILDISCO, DEBTOR-IN POSSESSION, ET AL.

AND

LOCAL 408, INTERNATIONAL BROTHERHOOD OF TEAMSTERS, CHAUFFEURS, WAREHOUSEMEN AND HELPERS OF AMERICA, PETITIONER (82-852)

v.

NATIONAL LABOR RELATIONS BOARD, ET AL.

On Writ of Certiorari to the United States Court of Appeals for the Third Circuit

BRIEF FOR PETITIONER, LOCAL UNION NO. 408, I.B.T.

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Questions Presented

1. Did the Court of Appeals err in holding that a debtor in possession of a reorganized business may obtain rejection of a collective bargaining agreement under the Bankruptcy Reform Act of 1978 §365(a), 11 U.S.C. §365(a), without requiring that the debtor in possession first comply with the bargaining requirement for mid-term contract modification contained in the National Labor Relations Act §8(d), 29 U.S.C. §158(d), prior to obtaining rejection under the Code?

2. Did the Court of Appeals err in ruling that a debtor in possession, who petitions for rejection of a collective bargaining agreement eight months after the debtor had filed for bankruptcy, is a new juridical entity which is not bound by the debtor's labor contract and not bound by the requirements of the labor laws during the period prior to obtaining rejection, even where, as here, all of the workers employed by the debtor in possession in the relevant unit had been employed by the debtor company and were covered by the collective bargaining agreement in effect between the debtor company and the union?

3. Did the Court of Appeals err in ruling that a petition to reject a labor contract under 11 U.S.C. §365(a) of the Bankruptcy Code may be granted merely after a weighing of the equities even where rejection is not necessary for the continued operation of the company and where the standard used by this Court of Appeals directly conflicts with the more stringent test established by the Second Circuit and followed by the lower courts?

List of Parties

The petitioner in No. 82-852 is Local 408, International Brotherhood of Teamsters, Chauffeurs, Warehousemen and Helpers of America (hereinafter ,"the Union"), the petitioner in the consolidated case No. 82-818 is the National Labor Relations Board (hereinafter, "the Board"), and the respondents in both cases are Bildisco (hereinafter, "Bildisco") and Bildisco, Debtor in Possession (hereinafter, Debtor in Possession).*

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* Case No. 82-852 arises out of the Union's appeal from the Bankruptcy Court's order granting rejection of the collective bargaining agreement. Case No. 82-818 arises out of the Board's effort to enforce its decision and order finding Bildisco and the Debtor in Possession guilty of an unfair labor practice. The cases were consolidated in the Court of Appeals and the Union and Board intervened in each other's case.

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Opinions and Judgments Below

The opinion of the Court of Appeals for the Third Circuit, entered on June 17, 1982, is reported at 682 F.2d 72 (3rd Cir. 1982) and is appended to the Union's petition for a writ of certiorari (Pa1 to Pa25).* The opinion of the District Court for the District of New Jersey was rendered on May 6, 1982, is unreported, and is appended to the Union's petition for a writ of certiorari (Pa28 to Pa34). The decision of the Bankruptcy Court was rendered on January 5, 1981, is unreported, and is included in the joint appendix submitted in connection with this brief (Ja56 to Ja77).** The Supreme Court of the United States granted a writ of certiorari in both cases on January 17, 1983.

Jurisdiction of the Supreme Court

Jurisdiction of this Court is conferred by 28 U.S.C. §1254(1) on grounds of a conflict in the courts of appeals and of the existence of issues of significant public import.

Statutes Involved

The statutory provisions involved in this case are the National Labor Relations Act, 29 U.S.C. §§151-169, specifically 29 U.S.C. §158(a) and (d), and the Bankruptcy Reform Act of 1978 (hereinafter, "Bankruptcy Code" or "Code"), 11 U.S.C. §§1-1330, specifically §356(a), 11 U.S.C. §365(a). No constitutional provisions are involved.

Statement of the Case

This matter arises out of a motion made in December 1980 by the Debtor in Possession, pursuant to 11 U.S.C.

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* "Pa" refers to the appendix attached to the petitioner Union's petition for a writ of certiorari.

** "Ja" refers to the joint appendix submitted in connection with this brief.

§365(a), to reject a collective bargaining agreement signed by Bildisco and the Union. Bildisco is a New Jersey partnership engaged in selling and distributing building supplies. Bildisco and the Union had been parties to a series of collective bargaining agreements, the most recent of which was effective from May 1, 1979 to April 30, 1982. That collective bargaining agreement expressly provided that it was binding upon the parties and their successors and that it remained binding even if the company went into bankruptcy (Ja91 to Ja92). Bildisco was not a party to any other labor contracts. Bildisco had at one time employed 18 persons in the unit covered by the collective bargaining agreement in effect with the Union. This number decreased to 3 employees by the date of the petition to reject the collective bargaining agreement. As of the date of the hearing on the motion to reject, all of the workers employed by the Debtor in Possession in the relevant work unit had been employees of Bildisco in that unit and had been covered by the collective bargaining agreement at issue. Several of the Union employees laid off by Bildisco and the Debtor in Possession had nearly 20 years of service to the company.*

Commencing in January 1980 Bildisco ceased making pension and welfare payments to the applicable trust funds on behalf of the employees covered by the collective bargaining agreement and also failed to forward to the Union the dues the company was withholding from the employees' pay checks. On April 14, 1980 Bildisco voluntarily filed for bankruptcy under chapter 11 of the Bankruptcy Code. The bankruptcy papers filed by Bisdisco contain no mention or suggestion of an intent to repudiate or reject the labor contract (Ja40 to Ja54). The bankruptcy court ap-

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* At the hearing on the petition to reject, one of the owners of the company (who was also a Debtor in Possession), stated that the company expected to have ten workers in the unit by the end of the next year (Ja59; Ja62). Approximately 40 to 45 percent of the company's labor rolls were covered by the Union contract (Ja59).

pointed the partnership as Debtor in Possession and authorized it to operate the business under 11 U.S.C. §1107. The Debtor in Possession continued to fail to make pension and welfare payments and to fail to forward to the Union the dues it deducted from the employees' pay checks. Several weeks later the Debtor in Possesion also failed to give the employees the raises called for by the collective bargaining agreement and denied them vacation pay (Ja79; Ja108 to Ja111). The Debtor in Possession never advised the Union or employees, orally or in writing, that it would not honor the labor contract or that it viewed itself as free from the terms of that contract. At no time did Bildisco or the Debtor in Possession seek to negotiate with the Union concerning changes in the collective bargaining agreement. In the summer of 1980 the Union filed unfair labor practice charges with the Board, alleging a violation of 29 U.S.C. §158(a) (1) and (5).

In December 1980 the Debtor In Possession petitioned the Bankruptcy Court under 11 U.S.C. §365(a) for rejection of the collective bargaining agreement. A hearing was held on January 5, 1981, after which the Bankruptcy Court promptly approved the petition to reject the labor contract. The Bankruptcy Court did not explain what standard it was using in approving rejection.

The Union appealed this decision to the District Court. The District Judge observed that under the superseded Bankruptcy Act judicial evaluations of petitions to reject contracts utilized a "business judgment" test for normal contracts and a more rigorous test for labor contracts. Accepting without comment the figures found by the Bankruptcy Court*, the District Court ruled that the contract

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*At the January 5, 1981 hearing the Debtor in Possession contended that rejection of the labor contract and the use of "non-union" workers would save the nearly $100,000 a year, which was slightly less than the predicted profits (Ja60). The Union, through cross-examination, contended that the savings would be approximtely $45,000, or less than half the predicted profits. See Union's briefs to Third Circuit. However, these factual disputes are not at issue in this appeal to this Court.

would have been rejected under either standard and it was therefore not necessary to determine which standard should apply. Accordingly, the District Court affirmed the Bankruptcy Court's decision approving rejection of the collective bargaining agreement in effect between Bildisco and the Union without deciding what standard of law applies. The Union then appealed to the Third Circuit.

Though neither the Union nor the Board contended that a collective bargaining agreement was exempt from the application of §365(a) of the Code, the Third Circuit commenced its decision by examining and rejecting the notion that a labor contract was outside the scope of §365(a). The court then analysed the standard which a court should employ in determining whether to approve rejection of NLRA contracts under §365(a).

The court noted that the standard for rejecting normal contracts is the "business judgment" test, whereby a contract may be rejected if the debtor in possession demonstrates that a more beneficial contract can be entered into (Pa12). The court also observed that under the superseded Bankruptcy Act the courts had established a more stringent test for rejection of labor contracts (Pa12). As the Third Circuit observed, this stricter test was first announced by a circuit court in *Local Union No. 455* v. *Kevin Steel Products Inc.*, 519 F.2d 698, 707 (2d Cir. 1975), in which the Second Circuit stated that rejection of a labor contract may occur after a "thorough scrutiny, and a careful balancing of the equities on both sides." The Third Circuit further noted that the Second Circuit subsequently expanded upon that standard by ruling that a labor contract may be rejected only where the debtor in possession shows both that rejection is necessary to save the debtor company from imminent collapse and that a balancing of the equities weighs in favor of the debtor. *BRAC* v. *REA Express, Inc.*, 523 F.2d 164, 169, 172 (2d Cir.), *cert. den.*, 423 U.S. 1017 (1975). The Third Circuit obliquely observed that the lower courts have followed the test as enunciated in *REA Express* (Pa13 to Pa14).

However, the Third Circuit expressly rejected the Second Circuit's test as stated in *REA Express,* castigating it as mere "gloss" upon, and the "illegitimate progeny" of, *Kevin Steel* (Pa13a; Pa16a). Instead, the Third Circuit declared that a labor contract may be rejected simply where the debtor in possession shows that the contract is "burdensome" and that rejection would "assist" in achieving a satisfactory reorganization (Pa16 to Pa17). Because the District and Bankruptcy Courts below had approved rejection of the labor contract without clearly stating the standard or the elements of the balancing, the District Court decision was reversed and the matter was remanded for further proceedings consistent with the Third Circuit's opinion.

Summary of Argument

(1)

The Third Circuit held that, automatically, immediately, and merely upon the initial filing for bankruptcy the debtor in possession is completely released from the debtor's labor contract and is free to unilaterally set its own terms and conditions of employment, even though the debtor in possession did not substantially alter the operation of the debtor or hire new employees. The basis for this spontaneous and premature liberation of the debtor in possession from the debtor's labor contract is found in the Third Circuit's "new entity" theory, under which the debtor in possession is deemed a separate and new juridical entity upon its appointment by the Bankruptcy Court pursuant to 11 U.S.C. §1107. The Third Circuit also analogized the debtor-in-possession to a "successor" and then stated that a successor is free from the predecessor's labor contract and may fix its own terms and conditions of employment, citing *NLRB* v. *Burns Security Services, Inc.,* 406 U. S. 272 (1972).

The Third Circuit's reasoning does not withstand scrutiny. The debtor in possession operates the same company doing the same business and, in this case, with the same employees. As the Eleventh Circuit recently stated, a debtor in possession cannot be deemed different from the debtor for purposes of the labor contract or labor laws. *Matter of Brada Miller Freight System,* Docket No. 82-7043 (11th Cir. 1983). To conclude that the appointment of a debtor in possession by a bankruptcy court creates an entirely different entity which is free from the debtor's obligations to its employees improperly glorifies hypertechnicality. *NLRB* v. *Baldwin Locomotive Works,* 128 F. 2d 39, 43-44 (3rd Cir. 1942).

Also erroneous is the analogy to a successor and the conclusion that a successor is always released from the predecessor's contract. Successorship law was designed to apply to situations where one company acquired or merged with another. *NLRB* v. *Burns, supra; John Wiley & Sons, Inc.* v. *Livingston,* 376 U. S. 543 (1964). However, here there is no merger, acquisition, or transfer of capital. Rather, the same party runs the same business. Moreover, a successor will be held to the predecessor's contract where it is perfectly clear that a majority of his employees worked for the predecessor and the successor has not expressly repudiated that contract. *NLRB* v. *Burns, supra*; *Howard Johnson Co.* v. *Detroit Local Joint Executive Board,* 417 U. S. 249 (1974). In this case the debtor in possession was the same person who owned the debtor company, employed the same workers performing the same jobs, and never gave notice that it repudiated the debtor's contract. Thus, even assuming the relevance of the successorship doctrine, this debtor in possession should have been held to the debtor's contract.

The Third Circuit's decision is also contrary to the law. There is nothing in either the Bankruptcy Code or the NLRA which supports the notion that the mere filing

for bankruptcy results in the automatic termination of the debtor's labor contract. On the contrary, those two statutes provide mechanisms to which a debtor in possession must adhere in order to modify or terminate a labor contract. The Code provides that a debtor in possession seeking to reject an executory contract must obtain the approval of the Bankruptcy Court. 11 U.S.C. §365(a). Until rejection is properly obtained by formal court order, the contract continues in full force. *Holtz* v. *Federal Reserve Bank of Kansas City*, 108 F.2d 216 (8th Cir. 1939); *In re Guardian Equipment Corp.*, 18 B. R. 864 (Bankr. S. D. Fla. 1982); 2 Collier on Bankruptcy ¶365.03 at 365-21 to 22 (15th ed. 1983).

Moreover, the automatic rejection of a labor contract violates the mid-term modification procedures contained in the NLRA. 29 U.S.C. §158(d). These procedures require the party seeking a modification in an existing contract to obtain the other party's consent to any change in the contract. *Oak Cliff-Golman Baking Co.*, 85 L.R.R.M. (BNA) 1035, 1036, 207 NLRB 1063, 1064 (1973), *enf'd*, 505 F.2d 1302 (5th Cir. 1974). As numerous courts have held, and by its own terms, (29 U.S.C. §152(1)), the NLRA applies to debtors in possession. There is no reason in law or logic to hold that a debtor in possession is bound by the labor laws but is mysteriously exempted from the debtor's contract.

The simultaneous application of the NLRA and the Code does not create a conflict; the two laws are capable of harmonious coexistence. However, substantial policy considerations dictate that compliance with the modification procedures in the NLRA should precede any effort to reject a contract under the Code. Congress has declared that industrial warfare is to be avoided by the use of the collective bargaining process. 29 U.S.C. §151. Resolution of labor disputes, including contract concessions, should be accomplished in the manner preferred by the legislature.

Moreover, utilization of the NLRA modification procedures would not hinder reorganization. If a debtor in possession were unable to obtain a union's consent to changes, it could then seek rejection under §365(a) of the Code. However, unless prerejection negotiation is required, there will be no opportunity for the union to preserve basic benefits and rights while agreeing to necessary concessions. Without the opportunity to negotiate modifications prior to rejection, industrial strife is inevitable. Therefore, this Court should rule that prior to obtaining rejection under the Code, a debtor in possession must first negotiate under §8(d) of the NLRA.

(2)

The Third Circuit held that rejection under §365(a) of the Code should be approved when a debtor in possession demonstrates that its labor contract is "burdensome" and where a weighing of equities shows that rejection will "assist" the rehabilitation of the company. In delineating this test the court eschewed the Second Circuit's test, enunciated in *BRAC* v. *REA Express, Inc.*, 523 F.2d 164, 172 (2d Cir.), *cert. den.*, 423 U.S. 1017 (1975), under which rejection may be granted only if necessary to avoid the collapse of the company. The Third Circuit's test improperly permits rejection even though it is not necessary for the survival of company or the preservation of jobs.

Unlike normal executory contracts, which may be rejected when they are shown to be burdensome, a labor contract is a unique agreement which governs the entirety of the workplace. Workers, unlike commercial adventurers, do not make momentary business deals. Rather, they are inextricably bound with management to the productive process and depend upon that relationship for salaries, vacations, pensions and health plans. Recognizing the importance of these rights, the Second Circuit limited rejection to those instances where it is necessary to preserve the

company and the jobs. *BRAC* v. *REA Express, Inc., supra.* The Third Circuit would allow rejection even though the workers' jobs are not in jeopardy, thereby needlessly sacrificing the workers' rights to expedite the company's recovery.

The Third Circuit's fear that a bankruptcy court could not adequately assess the impact of denial of rejection on the company is without merit. The lower courts have successfully applied the *REA Express* test since 1975. Moreover, the Code requires that elaborate and detailed financial statements and schedules be filed upon and after the filing for bankruptcy. Also, the reorganization plan and accompanying disclosure statement which form the heart of a chapter 11 reorganization provide full description of the estate's financial situation. These papers, and the bankruptcy court's ability to assess an estate, undermine any notion that those courts are incapable of determining whether denial of rejection will ruin the company. Because the courts are clearly able to assess the estate's financial condition, and because the *REA Express* test provides a more equitable and humane analysis of the relevant considerations, this Court should reverse the decision below in favor of the test described in *REA Express.*

POINT I

This Court should rule that, at least for purposes of labor laws and labor contracts, a debtor in possession is not automatically released from the debtor's contract merely upon the filing for bankruptcy; that a debtor in possession is bound by both the National Labor Relations Act and the Bankruptcy Code; that both the Code and the Labor Act prohibit the unilateral rejection of a labor contract and the unilateral imposition of new contract terms; and that significant policy considerations dictate that a debtor in possession wishing to modify a labor contract comply with the bargaining procedures in the Labor Act prior to obtaining rejection under the Code.

Congress has determined that the rights and responsibilities of a company in chapter 11 bankruptcy are simultaneously controlled by two statutes: the Bankruptcy Code and the National Labor Relations Act.* The Code contains a specific mechanism whereby a debtor in possession may reject an executory contract at any time prior to the confirmation of the reorganization plan by obtaining the approval of the bankruptcy court. 11 U.S.C. §365(a). The NLRA contains a system whereby a party to a collective bargaining agreement must negotiate with and obtain the consent of the other party prior to implementing mid-term modifications in that contract. 29 U.S.C. §158(d). Despite these express and unequivocal statutory provisions, the Third Circuit has ruled that a debtor in possession is completely emancipated from the company's

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* Specifically, Congress has declared that the NLRA applies to trustees in Chapter 11 bankruptcy. 29 U.S.C. §152(1) and (2). The applicability of the Code to Chapter 11 proceedings is self-evident. Significantly, the arguments in this case and in this brief deal only with a Chapter 11 reorganization, not a liquidation proceeding.

collective bargaining agreement, and free to unilaterally fix its own terms and conditions of employment, automatically and immediately upon the initial filing for bankruptcy. As a result of that decision, employees who have dedicated years of service to a company will lose their pension and welfare benefits, lose their seniority and attendant rights, lose the protections of the grievance resolution system, and suffer a reduction in wages, vacations and sick days without ever having had the opportunity to agree to mid-term concessions and without ever having had the chance to oppose a rejection petition. Simply stated, the procedures and protections conferred by Congress in the Code and NLRA have been eviscerated and disregarded by a court of appeals.

It is the Union's position that this utter destruction of the collective bargaining agreement upon the filing for bankruptcy, and the corollary grant to the debtor in possession of the awesome power to unilaterally impose whatever terms and conditions of employment it may wish, is contrary to both the NLRA and the Code. The Union contends that a debtor in possession is not distinguishable from the debtor company for purposes of labor contracts and labor laws and that a debtor in possession is bound by the debtor's labor agreement until it gains modifications or a termination in accordance with §8(d) of the NLRA or §365(a) of the Code. Finally, it is the Union's position that sound and substantial policy considerations, combined with canons of statutory construction, compel the conclusion that rejection under the Code should not be permitted unless the debtor in possession first complies with the negotiating procedures in §8(d) of the NLRA.

The Bankrupcty Code constitutes an extensive schema designed to permit and assist a financially distressed company to restructure its debt and arrange its operation so as to facilitate recovery. Though a chapter 11 reorganization is under the ultimate authority of the bankruptcy court, the debtor will normally continue to op-

erate the company as debtor in possession. 11 U.S.C. §§1101, 1107. See also H.R. Rep. 595, 95th Cong. 1st Sess. 220 at 232-234 (1977), reprinted in 1978 U.S. Code Cong. & Ad. News 5963. One device by which the debtor in possession may improve the company's economic condition is to reject an executory contract to which the debtor is a party. 11 U.S.C. §365(a).* If rejection is approved, the contract is deemed to have been breached as of the day before the initial filing for bankruptcy. 11 U.S.C. §365 (g).** A bankruptcy court faced with a petition to reject a contract under §365(a) cannot modify the contract. Rather, the court can only approve or deny the petition to reject the contract in its entirety, without compromises. *In re David A. Rosow, Inc.*, 9 B.R. 190, 193 n.5 (Bankr. D. Conn. 1981); 2 Collier on Bankruptcy ¶365.01[2] at 365-11 (15th ed. 1981).

On the other hand, the NLRA provides a mechanism whereby a party seeking to modify or alter an existing collective bargaining agreement may do so. 29 U.S.C. §158

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* 11 U.S.C. §365(a) of the Bankruptcy Code provides:

> "Except as provided in sections 765 and 766 of this title and in subsections (b), (c), and (d) of this section, the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor."

This Union does not dispute the authority of a bankruptcy court to ultimately reject a labor contract.

** 11 U.S.C. §365(g) states, in pertinent part:

> "(g) Except as provided in subsections (h)(2) and (i)(2) of this section, the rejection of an executory contract or unexpired lease of the debtor constitutes a breach of such contract or lease—
>
> (1) if such contract or lease has not been assumed under this section or under a plan confirmed under chapter 9, 11, or 13 of this title, immediately before the date of the filing of the petition; or"

(d).* Section 8(d) has been interpreted by the Board and the courts to permit a party to attempt to alter a contract in mid-term, even though more than 60 days remain in the

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*29 U.S.C. §158(d) provides in pertinent part that:

"(d) For the purpose of this section, to bargain collectively is the performance of the mutual obligation of the employer and the representative of the employees to meet at reasonable times and confer in good faith with respect to wages, hours, and other terms and conditions of employment, or the negotiation of an agreement, or any question arising thereunder, and the execution of a written contract incorporating any agreement reached if requested by either party, but such obligation does not compel either party to agree to a proposal or require the making of a concession: *Provided,* That where there is in effect a collective-bargaining contract covering employees in an industry affecting commerce, the duty to bargain collectively shall also mean that no party to such contract shall terminate or modify such contract, unless the party desiring such termination or modification—

(1) serves a written notice upon the other party to the contract of the proposed termination or modification sixty days prior to the expiration date thereof, or in the event such contract contains no expiration date, sixty days prior to the time it is proposed to make such termination or modification.

(2) offers to meet and confer with the other party for the purpose of negotiating a new contract or a contract containing the proposed modifications;

(3) notifies the Federal Mediation and Conciliation Service within thirty days after such notice of the existence of a dispute, and simultaneously therewith notifies any State or Territorial agency established to mediate and conciliate disputes with the State or Territory where the dispute occurred, provided no agreement had been reached by that time; and

(4) continues in full force and effect, without resorting to strike or lock-out, all the terms and conditions of the existing contract for a period of sixty days after such notice is given or until the expiration date of such contract, whichever occurs later."

contract's life. *Dunham-Bush, Inc.*, 111 L.R.R.M. (BNA) 1389, 1391, 264 NLRB No. 175 (1982); *Oak Cliff-Golman Baking Co.*, 85 L.R.R.M. (BNA) 1035, 1036, 207 NLRB 1063, 1064 (1973), *enf'd*, 505 F.2d 1302 (5th Cir. 1974). However, the party seeking a mid-term change may modify the contract only if it obtains the consent of the other party. *C&S Industries, Inc.*, 62 L.R.R.M. (BNA) 1043, 1045, 158 NLRB 454 (1966). If consent is not given, the contract may not be modified until, of course, it expires. A unilaterally imposed mid-term modification of a mandatory term of bargaining constitutes an unfair labor practice in violation of §8(a)(5) of the NLRA. *Chemical Workers* v. *Pittsburgh Plate Glass Co.*, 404 U.S. 157 (1971); *NLRB* v. *Katz*, 369 U.S. 736, 743 (1962).

Clearly, both the Code and the NLRA provide mechanisms whereby a debtor can obtain relief from an unduly oppressive labor contract, the former by petition to and approval by the bankruptcy court, the latter by mutual consent of the parties arrived at through collective bargaining. These two avenues of redress are not mutually exclusive. On the contrary, a debtor in possession can first attempt to alleviate the problems it perceives as caused by its collective bargaining agreement by negotiating pursuant to §8(d). If unsuccessful in arriving at a mutually agreeable modification with the union, the debtor in possession can then attempt to reject the contract by application to the bankruptcy court under §365(a). The two statutes are capable of amicable coexistence in a manner which adequately protects the interests served by both laws: industrial peace and corporate rehabilitation.

Rather than essay a reconciliation of the NLRA and the Code, the Third Circuit ruled that a company wishing to free itself from a labor contract may do so simply by filing in bankruptcy; it need not gain the union's consent through negotiation and it need not obtain rejection of the contract by a bankruptcy court. Simply and solely upon the filing for bankruptcy the unionized com-

pany becomes non-union, able to set its own terms and conditions of employment and able to fire and hire whomever it wants. Gone are the pension and health benefits, gone are the arbitration procedures, gone are the wages which the workers had been earning and upon which they pay for housing, cars and food.*

This automatic emancipation of a previously unionized company was not proclaimed by Congress or the President. It was decreed by a court of appeals. In explaining its decision freeing a debtor in possession from a labor contract merely upon the filing for bankruptcy and without regard to §8(d) or §365(a), the Third Circuit provided little more than conclusory statements. In two sentences (both adopted from the Second Circuit's seminal decision in *Shopmen's Local Union No. 445* v. *Kevin Steel Products, Inc.*, 519 F.2d 698 (2d Cir. 1975)), the Third Circuit stated that a debtor in possession:

> "is a new entity, separate and apart from the pre-bankruptcy company, and does not become a party to an executory contract unless it assumes the contract. Bildisco, as a debtor-in-possession, was not a party to the collective bargaining agreement, and therefore not bound by §8(d) [29 U.S.C. §158 (d)]." (Pa12).

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* These consequences which flow from the Third Circuit's decision are not the febrile speculations of a paranoid litigant exaggerating its case. These results are actually occurring. For example, as reported in the New York Times, the Wilson Foods Corporation, the nation's largest processor of pork, filed for bankruptcy under Chapter 11 on April 22, 1983. Two days later it unilaterally reduced its workers' wages by 40 to 50 percent and substantially reduced benefits. Less than a week later the company announced a new $80 million revolving credit agreement with Citicorp Industrial Credit, Inc. Lewin, *Business and the Law*, N. Y. Times, May 3, 1983, at D2, col.1. The remainder of the article suggests that companies may be using the bankruptcy laws for ulterior reasons. *Id.* Perhaps the Labor Board was prescient when, in *Kevin Steel*, it voiced concern that companies would misuse the bankruptcy laws to escape from unfavorable labor contracts.

The Third Circuit added that:

> "The debtor-in-possession's position is analogous to that of a successor employer: it may be required to recognize and bargain with the union, but it is not a party to its predecessor's collective bargaining agreement unless it assumes that agreement. *NLRB* v. *Burns Security Services Inc.*, 406 U.S. 272, 284 (1972); *Kevin Steel*, 519 F.2d at 704." (Pa20 to Pa21).

The Third Circuit's ruling that a debtor in possession is a completely new juridical entity freed from the bonds of the labor contract immediately upon the filing in bankruptcy is wrong as a matter of law and logic. Moreover, the Third Circuit's attempt to buttress its holding by comparing the debtor in possession to a successor, and then announcing that a successor is *always* exempted from the predecessor's contract, is too facile, for it is clear from this Court's decisions that a successor may be required to negotiate with the union *before* it can change the terms of the predecessor's labor contract.

As noted above, the Code provides that a debtor in possession may reject an executory contract by gaining the approval of the bankruptcy court. 11 U.S.C. §365(a). This requirement is not some superfluous prediliction but a specific statutory dictate. It is therefore hardly surprising that the courts have long and repeatedly ruled that a contract cannot be deemed rejected, and remains binding, until formal approval is conferred by a court. See, *e.g.*, *Holtz* v. *Federal Reserve Bank of Kansas City*, 108 F.2d 216, 219-220 (8th Cir. 1939) (as long as rejection is not ordered, the contract continues in existence); *In re Guardian Equipment Corp.*, 18 B.R. 864 (Bankr. S.D. Fla. 1982) (until debtor in possession obtained formal rejection in court, it remained bound to terms of lease entered by debtor); *In re Smith Jones, Inc.*, 17 B.R. 126, 128 (Bankr. D. Minn. 1981) (absent formal rejection under the Code, the terms of the

contract continue[d] in effect and were applicable to debtor in possession); *In re Eastern Fruit Company, Inc.*, 1 B.R. 714, 716 (Bankr. E.D. Pa. 1979). See also 2 Collier on Bankruptcy ¶365.03 at 365-21 to 22 (15th ed. 1983); D. Lynn, M. Rochelle and L. King, *Collier Handbook for Trustees and Debtors in Possession* (1982) ¶23.04 at 23-16 ("although collective bargaining agreements and union contracts may be subject to review by the Bankruptcy Court by the debtor's motion to reject, [footnote omitted] until the court may conduct such review they are in full force and effect.").

In view of the requirement in §365(a) that a debtor in possession obtain court approval for rejection of a contract, and in light of the decisions correctly concluding that the debtor's contracts remain binding upon a debtor in possession until the procedure in §365(a) is pursued, the Third Circuit's decision releasing the debtor in possession from the debtor's contract upon filing for bankruptcy must be seriously questioned. The question may be posed in two related forms: 1) if upon the filing for bankruptcy the debtor in possession is not bound by nor a party to the debtor's labor contract, then why does the debtor in possession need to petition for rejection at all? and 2) if the mere filing for bankruptcy liberates the debtor in possession from the debtor's contract, then why did Congress bother to provide a procedure requiring court approval for rejection and make the retroactive breach effected by §365(g) contingent upon approvad of rejection?* The import of these questions cannot be too strongly emphasized, for the Third Circuit's decision is nothing less than a judicial rewrite of a statutory plan.

The logical flaws in the new entity theory were quickly perceived even by its creator, the Second Circuit. Just

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* The problems emanating from the notion that a debtor in possession is a new entity distinct from the debtor raises problems in areas other than labor. For example, can the debtor in possession operate under licenses granted by state or federal agencies to the debtor, or must the debtor in possession obtain new licenses?

one year after *Kevin Steel* that circuit began revision. In *Truck Drivers Local Union No. 807* v. *Bohack Corp.*, 541 F.2d 312 (2d Cir. 1976) the court explained:

> "Of course, the statement that the debtor is not a party, and the analogy to the successor employer, cannot be taken literally since neither affirmance nor rejection of the collective bargaining agreement would be possible by one not a party to it."

Id. at 320.

Sounding a similarly narrowing theme, the Second Circuit subsequently cautioned the lower courts to limit the application of the new entity theory to those cases where the unions claim that the provisions of §8(d) pertain. *In re Matter of Unishops*, 543 F.2d 1017, 1018-1019 (2d Cir. 1976). Retreating even further from its own doctrine, the Second Circuit recently stated that a labor contract is binding upon a debtor in possession if it receives benefits under it. *In re W.T. Grant Co.*, 620 F.2d 319, 321 (2d Cir. 1980). In language pertinent to the instant case, the *W.T. Grant* court found the debtor in possession bound to the debtor's labor contract because:

> "Here, Grant received benefits under the contract by permitting the workers to continue in its employ after it entered Chapter XI. As the district court stated, Grant secured 'the services of an experienced Grant personel during the Chapter XI proceeding . . .'"

Id.

Other courts and legal commentators have also questioned the soundness of the new entity theory. In *In re Price Chopper Supermarkets, Inc.*, 19 B.R. 462 (Bankr. S.D. Cal. 1982) the court, observing that the "new entity" theory was not necessary to the decision in *Kevin Steel*, stated that:

> "This new entity theory has been critized for it creates the paradoxical situation that the debtor-in-possession is cast as a new employer, apparently not bound by preexisting executory contracts and yet, it must make an appropriate showing to reject such agreements, including satisfying the higher standard imposed when dealing with applications to reject collective bargaining contracts. *See Matter of Ryan Company, Inc.*, 4 B.C.D. 64, 65 (Conn. 1978); *Note, supra* 80 Mich. L. Rev. at 148 . . ."

Id. at 456. See also *In the Matter of Allied Supermarkets, Inc.*, 6 B.R. 968, n. 8 (Bankr. E.D. Mich. 1980) (and the law review articles cited therein).*

Perhaps the final blow to the new entity theory was dealt by the Eleventh Circuit in *Matter of Brada Miller Freight Systems, Inc.*, Docket No. 82-7043 (11th Cir. 1983), in which the court was confronted with the identical question of when and how a debtor in possession may reject the debtor's labor contract. The Eleventh Circuit observed that the Second Circuit had been continually restricting the new entity notion in a series of contrived decisions. *Matter of Brada Miller, supra,* slip op. at 2356-2357. More importantly, the court found the legal obstacles of §365(a) and (g) insurmountable, explaining that a theory which frees a debtor in possession from a contract without the need to obtain formal court approval violates the Congressionally arranged plan which mandates court-approved rejection and which makes retro-

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* Though most legal commentators have eschewed the "new entity" theory, one law review article took the position that the debtor in possession may be a new entity but that "regardless of the different legal status of the Debtor in Possession, its interest in the company is indistinguishable from the debtor's for the purpose of fulfilling the debtor's Labor Act obligations, and that the Labor Act intended to bind the trustee or debtor in possession to the debtor's obligations." Note, *Labor-Bankruptcy Conflict,* 80 Mich. L. Rev. 134, 139 n.29.

active release from the contract contingent upon approval of rejection.* *Matter of Brada Miller, supra,* slip op. at 2356. Finding the new entity theory both legally and logically defective, the Eleventh Circuit declared:

> "While we recognize that the debtor-in-possession may constitute a 'new juridical entity' for some purposes,[14] we find the debtor-in-possession indistinguishable from the pre-bankruptcy corporation as far as concerns their respective obligations under the collective bargaining agreement and the labor laws that regulate the formation, existence, and termination of such agreements."

Id. at 2355-2356. (footnote omitted).

The sound reasoning of the Eleventh Circuit also emphasizes the legally and factually erroneous conclusion of the Third Circuit that the debtor in possession is a "successor" and thus not bound by the debtor/predecessor's labor contract under the successorship doctrine. Just as the new entity theory was an untenable and invalid fiction formulated to achieve a desired result, so the analogy of a debtor in possession to a successor is neither appropriate nor useful.

The courts developed the successorship doctrine to deal with labor problems arising where one company merged with, acquired or replaced another company and yet retained a number of the predecessor's employees and performed substantially the same business operation. *NLRB* v. *Burns Security Services, Inc.*, 406 U.S. 272 (1972); *John Wiley & Sons, Inc.* v. *Livingston*, 376 U.S. 543 (1964). However, where, as here, the bankruptcy court appoints the

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* The Eleventh Circuit commented that the proponents of the "new entity" theory had yet to explain the paradox that theory creates when a petition to reject is denied and the debtor in possession is thus bound by the contract. As the Eleventh Circuit pondered, how can a non-party to the contract be held to the contract when rejection is denied?

debtor to continue to operate the company under the title of debtor in possession, there is no change in ownership nor transfer of capital. As the Eleventh Circuit properly stated, there is no difference for purposes of labor contracts between the debtor and the debtor in possession. *Matter of Brada Miller, supra.* Indeed, the Third Circuit previously stated that:

> "Court supervision of corporate reorganization affords the operating possessor no freedom from its statutory duty to its employees. And, where managerial control and economic interest of the debtor in possession and the [debtor] company are the same . . . then in no legally significant sense . . . can the [debtor] be differentiated from the debtor in possession so far as the employer-employee relationship is concerned."

NLRB v. *Baldwin Locomotive Works,* 128 F.2d 39, 43-44 (3d Cir. 1942). In short, application of the successorship doctrine to this case is neither warranted nor appropriate.

Even if successorship principles are applied here, it is patently evident that until it obtained rejection of the collective bargaining agreement in January 1981, this Debtor in Possession should have been bound by the terms of the labor contract and should have negotiated with the Union prior to changing the terms of that contract. As the Third Circuit stated, a debtor in possession is a "successor." Once that threshold question is resolved, however, the more complex inquiry concerns the extent, if any, of the successor's obligations under the predecessor's contract. The contours and content of this inquiry were delineated by this Court in two decisions, *NLRB* v. *Burns, supra,* and *Howard Johnson Co.* v. *Detroit Local Joint Executive Board,* 417 U.S. 249 (1974).

In *Burns* the predecessor company, Wackenhut, had provided security services at the Lockheed facility and was

party to a three-year collective bargaining agreement. Approximately one month after it entered into that collective bargaining agreement, Wackenhut was replaced by the Burns company, which had submitted a lower bid to Lockheed. Burns employed 27 of Wackenhut's workers and brought in 15 of its own employees from other facilities. The union claimed that Burns was bound by all of the terms of the collective bargaining agreement it had entered into the month before with Wackenhut. However, when it bid for the Lockheed job, Burns had made clear that it was not consenting to the Wackenhut labor contract. *NLRB* v. *Burns, supra* at 286. Emphaszing that, unlike in *Wiley,* Burns had not purchased or merged with Wackenhut but simply underbid a competitor, this Court noted that the sole basis for the union's contention that Burns was bound by the Wackenhut contract was that Burns hired enough of Wackenhut's employees to impose a bargaining relationship. *NLRB* v. *Burns, supra.* The Court found that factor an inadequate basis on which to hold Burns to all of the terms of the Wackenhut labor contract or to require it to negotiate prior to initiating changes in that contract. *NLRB* v. *Burns, supra* at 287, 294. However, and significantly, the Court added that:

> "Although a successor employer is ordinarily free to set initial terms on which it will hire the employees of a predecessor, there will be instances in which it is perfectly clear that the new employer plans to retain all of the employees in the unit and in which it will be appropriate to have him initially consult with the employees' bargaining representative *before* he fixes terms."

NLRB v. *Burns, supra* at 294-295. (emphasis added). The Court added that its holding also had the beneficial effect of furthering the transfer of capital, an important objective in a free economy. *NLRB* v. *Burns, supra* at 288-289.

In *Howard Johnson* v. *Detroit Local Joint Exec. Bd., supra,* this Court reminded companies and unions that the existence of a successor relationship, and the extent of the successor's bargaining duties, are factual questions which can only be determined on a case by case basis. *Id.* at 256. The *Howard Johnson* Court ruled that where the purchasing company expressly informed the seller in advance that it refused to adhere to the seller's collective bargaining agreement, where all of the seller's employees were notified that upon the sale of the company they would be terminated, and where the purchaser hired its own workforce (of whom only a small percentage had worked for the predecessor), then the purchaser was not bound by the seller's bargaining agreement and was not required to negotiate prior to setting its own terms and conditions of employment, even though the predecessor's contract provided that it was binding upon successors.*

Assuming, *arguendo,* that successorship theory is applicble where a debtor in possession replaces a debtor, the facts in this case make it readily apparent that this Debtor in Possesion was bound by Bildisco's collective bargaining

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* The *Howard Johnson* decision also made explicit what was implicit in *Burns,* to wit, a successor is not required to hire the employees of the predecessor and may recruit an entirely new workforce. *Howard Johnson Co., supra* at 261-262. Thus, under the "new entity" theory a debtor in possession (either as a non-party or successor to the contract) could terminate all of the debtor/predecessor's employees and hire a completely new workforce, as long as it does not fire/hire solely because of a person's union association. *Howard Johnson, supra* at 202 n. 8; *In re Unit Parts Co.,* 10 B.R. 970, 979 (Bnkr. W.D. Okla. 1981). When this right is viewed in connection with the Second Circuit's holding in *W.T. Grant, supra* (that a debtor in possession is bound by the debtor's labor contract because it continued to employ the debtor's workers), it becomes apparent that a debtor in possession has not only the authority but the inducement to terminate the debtor's employees immediately upon its appointment by the bankruptcy court under 11 U.S.C. §1107. This prospect is certain to cause industrial warfare.

agreement and should have negotiated before it changed any of its terms. When it filed for bankruptcy, Bildisco's papers contained no indication that it was rejecting or disavowing its collective bargaining agreement (Ja40 to Ja50). The bankruptcy court appointed the debtor as Debtor in Possession, meaning that the same persons who owned and operated Bildisco remained in place without change. There was no interruption or change in operation. The Debtor in Possession did not fire Bildisco's employees and hire new ones; it continued to employ the same workers in the same jobs performing the same duties as under Bildisco. In sum, there was no change in or replacement of the owners, managers, supervisors, employees, or the business and operations of Bildisco, other than a gradual reduction in the number of union employees. Moreover, the collective bargaining agreement entered into between Bildisco and the Union expressly provided that it applied to all successors, administrators and receivers, even if Bildisco went into bankruptcy (Ja91 to Ja92). At no point did Bildisco or the Debtor in Possession ever inform the workers that the Debtor in Possession was not bound by the terms of the contract or of its intent not to be bound by the contract.* Furthermore, there is no issue here of hinder-

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* In similar circumstances this Court observed that when a new employer acquires the assets of the predecessor and continues the predecessor's business without significant change in operations, the employees will understandably view their job situations as unchanged. *Golden State Bottling Co.* v. *NLRB*, 414 U.S. 168, 183 (1973). That view is even more reasonable when, as here, neither the union nor employees were told that the Debtor in Possession perceived itself as legally freed from the collective bargaining agreement. The respondents may argue that the failure to make pension and welfare payments upon the Debtor in Possession's appointment in April 1980, and the failure to give the required wage increases which were due in May 1980, amount to notice that it refused to adhere to the contract similar to the notice given

(Footnote continued on following page)

ing the transfer of capital through corporate mergers or acquisitions.* Under the successorship decisions of this Court, this Debtor in Possession was not only a successor but fell squarely within the circumstances noted in *Burns* under which the successor is required to negotiate with the union prior to implementing any changes in the collective bargaining agreement. *NLRB* v. *Burns*, 406 U.S. at 294-295.

That this Debtor in Possession was obligated to negotiate before effectuating changes in Bildisco's contract is consistent with recent decisions of the lower courts. For example,

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(Footnote continued from preceding page)

in *Howard Johnson*. However, the notice of repudiation in *Howard Johnson* was given before the acquisition and transfer of ownership, not after, and was in writing. This Union had no basis to believe that the failure to contribute to the funds constituted rejection of the contract because Bildisco had stopped making contributions in January 1980, four months prior to filing for bankruptcy. As with so many companies who are delinquent for months in contributions to the funds, the unions and/or funds eventually institute proceedings for delinquent payments but do not view the failure to pay as a disavowal of the contract. Finally, the failure to accord the workers the wage increases called for in the contract occurred several weeks after the filing for bankruptcy and is irrelevant here, for the Third Circuit's decision centers on the debtor in possession's rights as of the day of filing for bankruptcy, not several weeks later.

* The *Burns* rule facilitates the unimpeded transfer of capital by providing that if a company sells its business, the buyer would normally not be bound by the existing collective bargaining agreement. However, where a company files for bankruptcy there is no transfer of capital or assets. Moreover, the Bankruptcy Code provides ample statutory means by which the debtor in possession can alleviate the company's distressed condition, including a restructuring of the debt and court-approved rejection of contracts. It is not necessary to afford a company facing or in bankruptcy additional benefits by providing that the filing for bankruptcy itself frees the company from its labor contracts. See, *Note, Labor-Bankruptcy Conflict, supra* at 144.

in *Local 92* v. *Strabley Building Supply, Inc.*, 98 L.R.R.M. (BNA) 3025 (N.D. Ohio 1978) Strabley Inc. purchased the assets of Danson Inc., which had a collective bargaining agreement with a union and under which Danson was behind in payments to the pension and welfare funds. Strabley Inc. knew of the arrears, and when it purchased Danson Inc. it refused to make any payments to the funds. The *Strabley* court noted that the successor never signed a collective bargaining agreement with the union nor ever expressed in writing any intent to adhere to the predecessor's contract. Moreover, the court observed that, as in *Howard Johnson,* the existence in the predecessor's collective bargaining agreement of a provision declaring that the collective bargaining agreement was binding on any purchaser or successor was not, by itself, dispositive, *Local 92* v. *Strabley Building Supply, supra.* However, the court concluded that, given the existence of the successorship clause, combined with the failure of the purchaser to expressly repudiate the collective bargaining agreement, the successor would be bound to the contract. *Local 92* v. *Strabley Building Supply, supra* at 3030-3031.

A similar result was reached in *In re Plaza Mission Bottling Co., Inc.*, 14 B.R. 428 (Bankr. E.D. N.Y. 1981). In that case the Plaza Beverage Company was party to a collective bargaining agreement. After the company transferred away its canning operation and retained its bottling operation, the bottling operation went into bankruptcy, keeping most of its non-supervisory workforce and all of its supervisory personnel. The union then filed claims for unpaid wages and benefits, which the bankrupt opposed by contending that it was not bound by the prior collective bargaining agreement. Pointing to the continuity in operation and personnel between the debtor company and the bankrupt, the court found that a successor relationship existed. *In re Plaza Mission Bottling Co., supra* at 431. The bankrupty then argued that even if it were a successor, it was not bound by the substantive provisions of the prede-

cessor's labor contract. After carefully examining this Court's successorship cases, the *Plaza Mission* court concluded that a successor could, under certain circumstances, be held to the preexisting labor agreement. As the court explained:

> "Presence of the following factors have been found sufficient to hold that the successor employer has assumed its predecessor's labor agreement.
>
> "(1) the collective bargaining agreement contains a provision providing that said agreement would be binding upon the employer's successors;
>
> "(2) did the successor employer disclaim any obligation to honor the pre-existing collective bargaining agreements; and
>
> "(3) did the successor employer honor any of the provisions of the collective bargaining agreement."

Id. at 433.

Under the facts of the case before it, the *Plaza Mission* court found the successor bound to the terms of the predecessor's collective bargaining agreement. See also *NLRB* v. *World Evangelism, Inc.*, 656 F.2d 1349, 1355 (9th Cir. 1981) (where it is "perfectly clear" that the successor plans to retain subtsantially all of the predecessor's employees in the relevant unit, "the successor must consult with the union before altering terms and conditions" of the predecessor's labor agreement); *General Teamsters, Chauffeurs, and Helpers, Local Union No. 249* v. *Bill's Trucking Co.*, 493 F.2d 956, 961-963 (3d Cir. 1974) (where there is an absolute identity or substantial continuity of business between predecessor and successor, successor will be bound to predecessor's labor contract.).

In light of the foregoing it is evident that neither the provisions of the Code nor the principles of the successorship doctrine support the Third Circuit's declaration that a debtor in possession is liberated from the debtor's col-

lective bargaining agreement simply, solely, and spontaneously upon the filing for bankruptcy.

The emancipation of the debtor in possession from the debtor's labor contract upon the filing for bankruptcy also violates the NLRA. As noted above, the NLRA itself states that it applies to debtors in possession in chapter 11 bankruptcy proceedings. 29 U.S.C. §152(1). The courts, including the Third Circuit in its decision below, have repeatedly ruled that a debtor in possession is bound by the labor laws. *Truck Drivers Local Union No. 807* v. *Bohack Corp.*, 541 F.2d at 318-319; *Shopmen's Local Union No. 455* v. *Kevin Steel, supra; BRAC* v. *REA Express, Inc.*, 523 F.2d 164 (2d Cir.), *cert. den.*, 423 U.S. 1017 (1976); *Durand* v. *NLRB*, 296 F.Supp. 1049 (W.D. Ark. 1969); *In re Penn Fruit Co.*, 1 B.R. at 716. That a company in bankruptcy is subject to the labor laws is neither legally novel nor methedologically impracticable. *Nathansan* v. *NLRB*, 344 U.S. 25 (1952); *In re Tucson Yellow Cab Co.*, 112 L.R.R.M. (BNA) 2705 (9th Cir. B.A.P. 1983); *Matter of Shippers Interstate Services, Inc.*, 618 F.2d 9 (7th Cir. 1980); *In re Bel Air Chateau Hospital, Inc.*, 611 F.2d 1248 (9th Cir. 1979); *BRAC* v. *REA Express, supra;* 2 Collier on Bankruptcy ¶365.03, *supra.* The Third Circuit's liberation of the debtor in possession from the debtor's collective bargaining agreement has no support in the applicable statutes. Nowhere in the NLRA is there any suggestion or statement that a filing for bankruptcy or appointment of a debtor in possession automatically abrogates an existing labor contract. *Matter of Brada Miller, supra; NLRB* v. *Baldwin Locomotive, supra; In re Penn Fruit Co., supra.*

In sum, the debtor in possession is bound by the rules set forth in both the Code and the NLRA and must comply with those procedures before altering or ending the debtor's labor contract. If the debtor in possession unilaterally al-

ters a mandatory term or condition of employment before it obtains rejection, then it has committed an unfair labor practice violative of §8(a)(5) of the NLRA. 29 U.S.C. §158(a)(5).

Since both the Code and the NLRA provide mechanisms for dealing with the same contract, the obvious question is whether one mechanism must or should precede the other. Ample and important policy considerations, coupled with rules of statutory construction which frown upon judicial decisions which needlessly ignore one law in favor of another, compel the conclusion that compliance with the collective bargaining procedures delineated in §8(d) should be followed prior to and as a condition of obtaining rejection under §365(a). *Morton* v. *Mancari*, 417 U.S. 535, 550-551 (1974). See also Note, *Labor-Bankruptcy Conflict, supra* at 150-152.

As this Court has emphasized, the NLRA represents a carefully conceived and exhaustively arranged system designed to facilitate peaceful labor relations through negotiation. *Chemical Workers* v. *Pittsburgh Plate Glass Co., supra; United Steelworkers* v. *Warrior & Gulf Nav. Co.*, 363 U.S. 574 (1960). The NLRA specifies that it is the policy of this nation to protect commerce "by encouraging the practice and procedure of collective bargaining. . . ." 29 U.S.C. §151. As this Court previously explained, §8(d) was enacted in the 1947 amendments to the NLRA, and an "important theme" of those revisions was to stabilize collective bargaining agreements. *Chemical Workers* v. *Pittsburgh Plate Glass Co., supra* at 186. This Court then declared that:

> "The structure and language of §8(d) point to a more specialized purpose than merely promoting general contract compliance. The conditions for a modification or termination set out in paragraphs (1) through (4) [of §8(d)] plainly are designed to regulate modifications and terminations so as to facilitate agreement in place of economic warfare."

Chemical Workers v. *Pittsburgh Plate Glass Co., supra* at 187.

Given the indisputable import of the collective bargaining process, and in view of its origination in the legislative branch, the judiciary must proceed with utmost caution in arriving at a decision which would in theory or practice eviscerate the bargaining process. *NLRB* v. *American National Insurance Co.*, 343 U.S. 395, 401-404 (1952). The balance of power between unions and management was struck by Congress and is a matter of fundamental public policy, not to be restructured by the judiciary. *Teamster Union Local 20* v. *Morton*, 377 U.S. 252, 259 (1964). In fact, this Court has continually exhibited a proper deference to the labor laws. For example, in *John Wiley & Sons* v. *Livingston*, 376 U.S. at 548-550, this Court declared that a successor company which was not a party to the predecessor's labor contract would nonetheless be obliged to comply with the arbitration provisions in that contract. The *Wiley* Court found that it would derogate from the policies of the labor laws if a change in the corporate structure or ownership of a company had the automatic result of removing the contractual duty to arbitrate to which the prior company had agreed. *Id.* at 549.

The precepts expressed and inherent in *Chemical Workers*, in *American Nat'l Insurance*, and in *Wiley* are applicable here. The bargaining process is central to labor relations and must be retained whenever possible. Requiring a debtor in possession to adhere to the bargaining provisions set forth in §8(d) would preserve the method of labor relations preferred by Congress. If a debtor in possession (or the debtor before filing for bankruptcy) desires a less onerous labor agreement, it should fully inform the union of its financial straits and the modifications necessary for the successful operation or rehabilitation of the company. Though a union faced with the facts

and figures may insist on the existing terms of the agreement, it is likely that the union will agree to a mutually satisfactory modification, thereby precluding the need for the debtor in possession to seek rejection. Though the debtor in possession may be in a seriously weakened economic condition, it does have the significant advantage which attaches to its ultimate weapon: **rejection.**

A union which adamantly refuses mid-term concessions faces the prospect that the company will obtain rejection of the contract. If the contract is rejected the union may find itself no longer representing the employees at the plant, and the employees will find themselves with lower wages, no pensions or welfare benefits, no seniority rights, no arbitration procedures, and no holiday or sick days. Certainly Bildisco's employees suffered a similar fate. Thus a debtor in possession should be required to comply with the negotiating provisions of §8(d). If unsuccessful in its effort to gain the union's consent to concessions, then the debtor in possession may seek refuge in rejection.

If application of §8(d) to a debtor in possession threatens the survival of the estate or imperils successful rehabilitation, the debtor in possession can apply to the bankruptcy court for protection. *In re Tucson Yellow Cab Co., supra* at 2707; *In re Bel Air Chateau Hospital, Inc., supra* at 1251. The bankruptcy court could either order an expedited negotiation schedule or, in extreme cases, waive the §8(d) procedures in their entirety. *In re Tucson Yellow Cab Co., supra;* Note, *Labor-Bankruptcy, supra* at 150. However, §8(d) is simply not so time consuming as to cause problems due to delays.*

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* Section 8(d) is not nearly as slow and elaborate as the contract modification procedures in the Railway Labor Act. 45 U.S.C. §156. Indeed, this Court observed that the mid-term bargaining steps contained in the RLA (§156) were purposely designed to be cumbersome and lengthy so as to allow the parties to cool-off and minimize the chances of a strike in the railroad industry. *Shore Line R.R.* v. *Transportation Union,* 396 U.S. 142, 143 (1969).

However, it is unlikely that the bankruptcy courts will often be asked to interdict or restrict the §8(d) procedures. A review of the reported cases concerning rejection of labor contracts reveals that, as in the instant case, many petitions to reject are made months, if not years, after the filing in bankruptcy.* See, *e.g., Local Union No. 455* v. *Kevin Steel, supra* (company filed in bankrupcty in September 1973 and later petitioned for rejection of labor contract, which was granted in March 1974); *In the Matter of Ryan Co., Inc.*, 4 B.C.D. 64 (Bankr. D. Conn. 1978) (company filed for bankruptcy on July 29, 1977, applied to reject labor agreement on January 11, 1978, and rejection was approved on March 10, 1978); *Bohack Corporation* v. *Teamsters, Local 807*, 431 F.Supp. 646 (S.D. N.Y. 1976) (company filed for bankruptcy on July 30, 1974 and rejection of labor contract was approved on May 28, 1976).

Moreover, recent history shows that a union requested to alter a contract will, out of sheer self-preservation, accede to mutually agreeable modifications. One need look no further than the daily papers to see that unions, recognizing the harsh realities of the current economic climate and the trend of companies to relocate in an effort to reduce labor costs, will agree to reductions in wages, to forego raises, to alter expensive work rules, and to reduce vacations and benefits in an effort to keep the company operating and the employees working. For example, the Transport Workers Union ratified a contract with American Airlines which provides for job security and wage increases, but which also eliminates paid meal periods, relaxes rules regarding utilization of employees in dif-

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* Rejection under §365(a) is available to a debtor in possession at any time prior to the confirmation of the plan. 11 U.S.C. §365 (d)(2); 2 Collier on Bankruptcy ¶365.03 at 365-19 (15th ed. 1983). Many months may elapse before the debtor even files a plan, no less gains confirmation of it. See 11 U.S.C. §1121. See also D. Epstein and J. Landers, *Debtors & Creditors* (2d ed. 1982) at 525.

ferent jobs, and slows progression up the wage scale. 112 L.R.R. (BNA) 202. The United Steelworkers have agreed to an industrywide contract which calls for an immediate pay cut of $1.31 per hour, elimination and reduction of future wage increases and cost-of-living increases, and the end of extended vacation and bonuses. 112 L.R.R. (BNA) 180. Indeed, the Steelworkers have adopted a two-tiered approach to contracts, under which special concessions are to be afforded financially distressed facilities. 112 L.R.R. (BNA) 68-69. At the Wheeling-Pittsburgh Steel Corporation, the Steelworkers agreed to concessions whereby the workers accepted a $1.53/hour cut in pay, deletion of cost of living increases in 1983, deletion of the dental insurance plan, and a loss of one week of vacation for employees now entitled to three weeks vacation each year. 112 L.R.R. (BNA) 22. Similar concessions mark numerous other contracts. See, *e.g.*, 110 L.R.R. (BNA) 3, 83; 109 L.R.R. (BNA) 213, 214, 228, 229, 321.

The point is that a prerejection bargaining requirement allows the parties to modify or eliminate the most burdensome contract terms while preserving provisions which protect fundamental interests of the workers. For example, in *In re Southern Electronics Co., Inc.*, 23 B.R. 348 (Bankr. E.D. Tenn. 1982) the company stated that it could live with the contract's wage rates but found the seniority rules unmanageable because they allegedly restricted the company's ability to terminate unproductive senior workers. The myriad factors which bear on cost and efficiency are susceptible of numerous possible compromises. The parties are limited only by their imaginations, guided by their respective needs. However, if a debtor in possession is freed from the collective bargaining agreement upon the filing for bankruptcy or is permitted to obtain rejection of the collective bargaining agreement without first negotiating, then there is no opportuntiy for the parties to even attempt to devise a mutually agreeable concession contract which would at least maintain some of the basic benefits for the workers.

The bargaining steps contained in the NLRA and the rejection procedure in the Code are clearly capable of harmonious coexistence. Where two statutes apply to the same situation and are capable of coexistence, a court should not ignore one. *Morton* v. *Mancari*, 417 U.S. at 550-551. In this case the concordance can be achieved by requiring bargaining before rejection. Indeed, to permit rejection without prior negotiations would needlessly and improperly derogate from the fundamental rights embodied and prescribed in the labor laws. Note, *Labor-Bankruptcy Conflict, supra* at 149-152. The inevitable consequence of allowing a debtor in possession to reject a labor contract without first having negotiated is industrial strife.

If this Court concludes that a debtor in possession is not required to comply with §8(d) before it imposes its own terms and conditions of employment, it is submitted that this Court should, at the very least, rule that negotiation with the union is a central and crucial consideration to be accorded substantial weight in a bankruptcy court's determination whether to approve rejection. Without the opportunity to agree to contract changes which reduce the company's costs while retaining essential benefits and protections, the workers will be subjected to terms and conditions of employment determined exclusively by management. It can hardly be expected that a debtor in possession freed from the debtor's contract would continue the wage rates, pension and health plans, and fringe benefits which the company had been providing. Surely the employees who have dedicated long years of service to the company deserve more than to be at the mercy of management without the opportunity to negotiate concessions in the contract. Contrary to the implication of the Third Circuit, employees are not on the same footing as a company's normal commercial creditors. Unlike a business which enters into a contract to supply parts, the workers under a union contract are an inextricable component of the company's production process. *United Steelworkers* v. *Warrior & Gulf Nav. Co.*, 363 U.S. at 578-579.

The appellate and trial courts have noted their preference for prerejection negotiation. As the bankruptcy court in California recently stated:

> "Thus, in all but the most extreme cases, the debtors-in-possession, or Chapter 11 trustees, should be required to move cautiously and bargain in good faith with their unions, in an attempt to foster a cooperative attitude in working towards a successful reorganization. This attempt at renegotiation should occur before coming before the court to achieve a unilateral rejection. [footnote omitted]. Obviously, in cases where the survival of the business itself is at stake, the urgent need to reject will require immediate action. In such cases, the required bargaining process will, by necessity, be kept to a minimum."

In re Price Choppers Supermarkets, Inc., 19 B.R. at 466. See also *Matter of Brada Miller supra*, slip op. at 2362; *In re Alan Wood Steel Co.*, 98 L.R.R.M. (BNA) 2400, 2401 (E.D. Pa. 1978).

The applicability of both the NLRA and the Code to a debtor in possession, the strong public and statutory policy favoring resolution of industrial problems through negotiation and agreement, and the simple fairness of allowing the union to negotiate a concession contract all combine to compel the conclusion that a debtor in possession should be required to follow the bargaining system set forth in §8(d) prior to obtaining rejection under §365(a). However, if adherence to §8(d) is not established as a mandatory condition precedent to rejection, it should be established as a central and critical consideration to be given great weight by a bankruptcy court. Indeed, if the debtor in possession has not engaged in prerejection negotiations under §8(d), rejection should be permitted only where absolutely necessary to avoid the imminent collapse of the company.

While the concerns addressed by the bankruptcy laws are unquestionably important, the purposes underlying the

labor laws are equally essential. To allow a company to unilaterally free itself of the collective bargaining agreement would not only contravene the provisions of the labor laws, it instills in the worker the ill feeling "that he is a pawn in industr[illegible]bject to the arbitrary power of the employer." *NLRB* v. *Highland Park Mfg. Co.*, 110 F.2d 632, 638 (4th Cir. 1940).

POINT II

This Court should reverse the standard for rejection adopted by the Third Circuit because it allows for rejection of a labor contract under the Code simply upon a showing that the contract is burdensome and that rejection will ease the estate's recovery; instead, this Court should adopt the test stated by the Second Circuit, which would allow rejection only where necessary to avoid the collapse of the company and the corollary loss of jobs.

Whether this Court concludes that rejection of a labor contract may be entertained only after the requirements of §8(d) are followed or concludes that prior negotiation is a crucial and significant factor which should be afforded substantial weight in a bankruptcy court's evaluation of a petition to reject the labor contract, the Union acknowledges that a bankruptcy court may ultimately adjudicate a petition to reject a labor contract. However, the evaluative process for rejection adumbrated by the Third Circuit is totally inadequate, for it permits rejection simply where it would "assist" a rehabilitation. The Third Circuit's standard suffers from the cruel shortcoming that it would sacrifice all of the workers' rights and protections even though not necessary for the company's continued operation and the continued employment of the workers. In arriving at this test, the Third Circuit declined to follow the more rigorous (and appropriate) test established by the Second Circuit, under which rejection would

be allowed only where necessary to the continued operation of the company and thus to the preservation of jobs. *BRAC* v. *REA Express, Inc.*, 523 F.2d 164, 172 (2d Cir.), *cert. den.*, 423 U.S. 1017 (1975).

Before examining the standard adopted below and comparing it to the more stringent test enunciated by the Second Circuit, it is helpful to examine the nature of collective bargaining agreements so as to better understand the ramifications of rejection. As this Court succinctly stated:

> "The collective bargaining agreement states the rights and duties of the parties. It is more than a contract; it is a generalized code to govern a myriad of cases which the draftsmen cannot wholly anticipate . . . The collective agreement covers the whole employment relationship. It calls into being a new common law—the common law of a particular industry or of a particular plant . . .
>
> . . . A collective bargaining agreement is an effort to erect a system of industrial self-government. When most parties enter into a contractual relationship they do so voluntarily, in the sense that there is no real compulsion to deal with one another, as opposed to dealing with other parties. This is not true of the labor agreement. The choice is generally not between entering or refusing to enter into a relationship, for that in all probability preexists the negotiations. Rather it is between having that relationship governed by an agreed-upon rule of law or leaving each and every matter subject to temporary resolution dependent solely upon the relative strength, at any given amount of contending forces."

United Steelworkers v. *Warrior & Gulf Nav. Co.*, 363 U.S. at 578-579.

The rights created and affected by a labor contract are two-fold: the rules which maintain order at the workplace and the rules which guarantee economic security to the workers. Among the former are seniority, grievance-arbitration procedures for dispute resolution, disciplinary procedures, and no-strike/no lock-out clauses. Among the latter are welfare and pension plans. Unlike a normal commercial contract, a collective bargaining agreement is an organic being whose terms are gleaned not merely from its express clauses but also from the history of relations between the workers and the company. *John Wiley & Sons* v. *Livingston*, 376 U.S. at 550. Furthermore, the rights and benefits earned by the workers are not measured by the existence of any one contract; rather, those rights and benefits derive their value from the expectation that the parties will continue to sign and adhere to successive labor contracts guaranteeing the pension and seniority rights accrued during any single contract.

Rejection of a labor contract means nothing less than termination of pension and health plans, reduction in wages, termination of all benefits such as vacation and sick days, and termination of the grievance resolution procedures within the workplace. Discussing the impact of rejection, the Second Circuit observed that it means "depriving the employees affected of their seniority, welfare and pension rights, as well as other valuable benefits which are incapable of forming the basis of a provable claim for damages." *Shopmen's Local No. 455* v. *Kevin Steel*, 519 F.2d at 707 (quoting from *In re Overseas National Airways, Inc.*, 238 F.Supp. 359, 361 (E.D. N.Y.

1965)).* The courts have continued to note that workers cannot obtain an adequate, or any, remedy when a labor contract is rejected. *Matter of Brada Miller, supra,* slip. op. at 2361; *In re Southern Electronics Co., Inc., supra* at 363. See also *Suffin* v. *Unity Button Works, Inc.,* 258 N.Y. 863, 864, 144 Misc. 7 84 (N.Y. Sup. Ct. 1932) (where employer disregarded contract and fired union workers, the damage was irreparable not only because of harm to workers but also because "the union loses in prestige and trade unionism in attractiveness, an injury incapable of compensation.").

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* Under the Code, the rights of workers and unions to payments are as follows: all claims for services rendered before 90 days prior to the initial filing for bankruptcy are general unsecured claims which have no statutory priority. Claims for wages, salaries, and vacation, severance and sick pay earned within 90 days before the filing for bankruptcy receive third priority as unsecured claims. 11 U.S.C. §507(a) (3). Claims for contributions to employee benefit plans arising from work performed within 180 days before the filing for bankruptcy are accorded a fourth priority as unsecured claims. 11 U.S.C. §507(a)(4). Wages and benefits earned during the reorganization period are deemed administrative expenses, which are given first priority. 11 U.S.C. §507(a)(1). However, and significantly, once a contract is rejected, it is deemed breached as of the *day before* the filing for bankruptcy. 2 Collier on Bankruptcy ¶365.08 at 365-40 to 41 (15th ed. 1983), 11 U.S.C. §365(g)(1).

In 17,282 asset cases concluded during the fiscal year, ending June 30, 1976, 14.5 percent of the total allowed claims were paid. Debtors satisfied 64.3 percent of secured claims, 29.6 percent of priority claims, and 6.5 percent of general unsecured claims. D. Epstein & J. Landers, Debtors and Creditors (1978) at 629. Of course, all claims for wages or fund contributions, even if afforded a priority, are unsecured and thus payable only after secured claims are paid in full. Also, the amount of wages and benefit plan contributions given priority status is severely restricted. Under 11 U.S.C. §507(a)(3)(B) each employee's priority claim is limited to $2,000.00. Moreover, the amounts protected under 11 U.S.C. §507(a)(4) are limited to the number of employees times $2,000, *minus* payments made as wage priority payments or to other benefit plans. D. Epstein & J. Landers, *Debtors & Creditors* (2d ed. 1982) at 563-564; 3 Collier on Bankruptcy ¶507.04 at 507-40.8 to 41 (15th ed. 1983).

In light of the drastic and irremediable consequences attending rejection of a labor contract under which the workers have given years of service, it is understandable that most courts have been extremely cautious in approving rejection. In the first appellate consideration of this issue, the Second Circuit declined to apply the normal test for rejecting commercial contracts and, instead, stated that rejection may be authorized "only after a thorough scrutiny, and careful balancing of the equities on both sides . . ." *Shopmen's Local 455* v. *Kevin Steel, supra* at 707.* However, the *Kevin Steel* test contained little content with which to guide the lower courts. Note, *Bankruptcy Law-Labor Law, Rejection of Collective Bargaining Agreements As Executory Contracts in Bankruptcy,* 22 Wayne L. Rev. 165, 176 (1975).

Shortly after the *Kevin Steel* decision, the Second Circuit clarified and reinforced the test. In *BRAC* v. *REA Express, Inc.,* 523 F.2d at 172, the court explained that "in view of the serious effects which rejection has on the [debtor's] employees," rejection would be permissible

> "only where it clearly appears to be the lessor of two evils and that, unless the agreement is rejected, the [company] will collapse and the employees will no longer have their job."

In cases involving petitions to reject labor contracts made under both the superseded Bankruptcy Act and the new Code, the lower courts have applied the test as delinated in

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* Under the normal test, called the "business judgment" test, an executory contract may be rejected where an existing contract can be replaced with a more profitable one or where the debtor in possession shows that the existing contract is burdensome. *Matter of Brada Miller, supra,* slip op. at 2359; 2 Collier on Bankruptcy 15th ed., *supra,* ¶365.03 at 365-14. According to Collier, the leading case in defining the test for normal contract rejection is *Group of Institutional Investors* v. *Chicago, Milwaukee St. Paul & Pacific R.R. Co.,* 318 U.S. 523, 549-551 (1943).

REA Express. See, *eg., In re Figure Flattery, Inc.,* 88 Lab. Cas. (CCH) ¶11,850 (S.D.N.Y. 1980); *Matter of Allied Technology, Inc.,* 8 B.R. 366, 368 (S.D. Ohio 1980); *Matter of Allied Supermarkets, Inc.,* 6 B.R. 968 (E.D. Mich. 1980); *Bohack Corp.* v. *Local Union No. 807,* 431 F.Supp. 64 (E.D. N.Y.), *aff'd,* 567 F.2d (2d Cir. 1977), *cert. den.,* 439 U.S. 825 (1978); *In re Alan Wood Steel Co.,* 449 F. Supp. 165, 169 (E.D. Pa. 1978), *appeal dismissed,* 595 F.2d 1211 (3d Cir. 1979); *In re Penn Fruit Co.,* 92 L.R.R.M. (BNA) 3548 (E.D. Pa. 1976); *In re Studio Eight Lighting,* 91 L.R.R.M. (BNA) 2429 (E.D. N.Y. 1976); *In re David Rosow, Inc.,* 9 B.R. at 192-193; *In the Matter of the Connecticut Celery Co.,* 106 L.R.R.M. (BNA) 2847 (Bankr. D. Conn. 1981).

Unmoved by the prospect of vast numbers of this nation's workers innocently losing pension, health and seniority benefits and suffering substantial reductions in wages as a consequence of often incompetent management, and unconvinced of the practicality of the strict standard applied by numerous courts which deal first hand with the intricacies of reorganization, the Third Circuit scorned the *REA Express* case, denouncing it as improper "gloss" on and the "illegitimate progeny" of *Kevin Steel* (Pa13 n.11; Pa16). In place of the *REA Express* test, which would sacrifice the workers' benefits only when the alternative was the loss of jobs, the Third Circuit embraced a lax "weighing of equities" test. Worse, the nature of the considerations recited by the Third Circuit, and the level at which the scale is to tip in favor of rejection, is essentially indistinguishable from the business judgment test utilized for normal commercial contracts.

In order to obtain rejection in the Third Circuit, the debtor in possession need only demonstrate that the labor contract is "burdensome" to the estate and then present sufficient facts to allow the court to determine whether rejection would "assist" in the rehabilitative process (Pa16 to Pa17). The Third Circuit recommends that in examining the various concerns of the parties, a court should

compare the rights of the covered employees to the sacrifices which other creditors are making (Pa16). In the final analysis, the bankruptcy court should approve rejection where that "will assist the debtor in possession or trustee to achieve a satisfactory reorganization." (Pa16 to Pa17).

The close kinship between the Third Circuit's test and the business judgment test is manifest. Under the Third Circuit's analysis, a labor contract may be rejected where a) the contract is "burdensome," b) the sacrifices of all creditors are considered and apportioned appropriately, and c) the rejection will "assist" the reorganization. In the "business judgment" test a contract may be rejected where a) the contract is burdensome, b) the sacrifice of all creditors are considered and apportioned appropriately, and c) the rejection would benefit the estate. *Institutional Investors* v. *Chicago, M., St. P. & P.R.R. Co.*, 318 U.S. at 549-550. Interestingly, the only case cited by the Third Circuit in its description of its test is *Institutional Investors* v. *Chicago, M. St. P. & P.R.R. Co.* (Pa16). Despite its contention that it was distilling out the impurities from the Second Circuit's test, the Third Circuit has gone further. Its alchemy has so altered the atoms that what was once *Kevin Steel* is now *Bildisco* rubber.

Of course, the issue is not the name attached to the standard but its content and workability. In defending its test the Third Circuit offered two rationales: that it may be impossible for a bankruptcy court to predict the success of a reorganization until very late in the arrangement proceedings, and that the *REA Express* test exhalts the contract over the question whether the workers will have jobs at all (Pa14). Neither of these reasons withstands examination.

Despite the fears of the Third Circuit, the lower courts have found the *REA Express* test entirely workable. The long list of cases adhering to *REA Express* noted above demonstrates, without more, that bankruptcy courts are

capable of predicting whether rejection is necessary to the continued operation of the debtor company. This prognostic ability is hardly surprising, for the Code not only allows but requires the early submission of detailed lists and schedules and then the filing of an elaborate reorganization plan and disclosure statement.

When a company files in bankruptcy under chapter 11 it must file a schedule containing a list of all creditors and of all assets. 11 U.S.C. §521(1). Some districts also require the initial lists to contain a summary of secured, priority, and unsecured debts and a projected operating statement for the 30 days following filing. *Collier Handbook, supra,* ¶21-06 at 21-15. If the debtor has a cash problem, it may have a hearing whereby it shows that a lender is adequately protected by proving that there is an equity cushion or by providing additional liens. 11 U.S.C. §§361, 363(e). Shortly after filing in chapter 11 the debtor in possession must file schedules of debts, executory contracts, and a list of equity security holders. 11 U.S.C. §521. Schedules must be filed relating to: priority debts under §507(a)(3)-(6); secured creditors (including the type of security involved, its value, and the amount secured); unsecured creditors; real property and any liens encumbering such property; personal property (including cash, bank accounts, furnishings and equipment, trucks and other vehicles, machinery and fixtures, inventory, patents and other intangibles, bonds, negotiable and non-negotiable instruments, liquidated debts owed to debtor, unliquidated claims, insurance policies, annuities, stock in other companies, and interests in partnerships); all other property; and all exempt property. See *Collier Handbook, supra,* ¶22.01 and 02, at 22-1 to 22-13. Also, the debtor in possession files a statement of financial affairs which provides a detailed explication of the company's operation. *Id.*

Of course, the plan forms the heart of a reorganization. The plan divides creditors into classes and spells out, ***inter alia,*** how each class is to be treated, how the plan is to be

executed, and how executory contracts are treated. 11 U.S.C. §§1121, 1123. The debtor in possession must also prepare a disclosure statement which is designed to provide creditors with sufficient information for making an informed judgment concerning the plan and its likelihood of success. 11 U.S.C. §1125(b), (d) and (e). The disclosure statement outlines the nature and history of the business, the risks inherent in the plan, the timing of the expected recovery, any options available, an analysis of the claims so that the assets can be determined accurately, and any other matter which should be brought to the attention of an interested party. *Collier Handbook* ¶25.10 at 25-47 to 25-54. The disclosure statement must be approved by the court at a hearing. 11 U.S.C. §1125(b).

The very purpose of the various lists, plan, and the disclosure statment is to permit the interested parties, the creditors' committee, and a court to make an educated evaluation of the operation of the company and the success of the proposed plan. Plainly stated, the Third Circuit's unsupported assertion that a bankruptcy court could not adequately assess the impact which denial of rejection would have upon the estate is contradicted by both the elaborate filing and plan requirements of the Code and by the proven ability of the courts to evaluate petitions to reject under the *REA Express* standard.

Also meritless is the Third Circuit's second objection to the *REA Express* test: that it exhalts the contract over jobs. This is simply not true. In order for a debtor in possession to obtain rejection under *REA Express* it must demonstrate that the denial of rejection will cause the imminent collapse of the company, thereby destroying the workers' jobs. Indeed, the *REA Express* test focuses the inquiry on whether denial of rejection will cost jobs. If the debtor in possession fails to show that rejection is necessary to the continued operation of the company, then rejection is not necessary to save the workers' jobs and rejection would plainly be inappropriate. See, Note,

Bankruptcy and the Rejection of Collective Bargaining Agreements, 51 Notre Dame Law. 819, 832 (1976) ("*REA Express* test is a "workable compromise" between the interests of the labor laws and bankruptcy laws which "takes into account the unique nature of the collective bargaining agreement as an embodiment of tangible and intangible human rights" in a manner which "does not preclude or hinder corporate reorganization . . .").

Succinctly stated, the *REA Express* test stands for this principle: where a debtor company can continue to operate without requiring that the workers surrender accrued benefits and wages, then fairness precludes a court from approving rejection and needlessly depriving those workers of pension, health and other benefits. In fact, to allow rejection even when it is not essential to the continued operation of the company would wrongfully promote the interests of the estate over those of the workers. Frankly, workers are not similarly situated to other creditors and should not be asked to sacrifice in the same manner as other creditors. Rather, workers have an inextricable and ongoing relationship with the company and should be protected so long as such protection does not entail the demise of the company and the jobs it provides.

To be sure, a job without benefits is better than no job at all, but that is a false issue. The *REA Express* test only states that if the company can continue with the labor contract then it should do so. Contrary to that, the Third Circuit would needlessly allow for the destruction of salaries, vacation and sick days, pensions, and health plans simply to "assist" a debtor return to health. While it is regettable that the Second Circuit did not adequately articulate the appropriate standard in its initial grapple with this issue, that should not detract from the propriety of the reconsideration it enunciated in *REA Express*. A second child, even if illegitimate, may be wiser than the first born.

The respondents may argue that labor contracts covered by the NLRA should not be accorded any special consideration because Congress, by inaction, has declined to favor them. This proposition has two themes. First it is argued that when Congress enacted §365(a) in 1978 it altered the previous provision by conferring special treatment on various lease contracts. By providing benefits to some contracts, so the argument runs, Congress knew how to afford similar consideration to labor contracts but failed to do so, thereby allegedly evincing an intent that labor contracts be treated as normal contracts. The other, similar version of this argument is that Congress expressly exempted the wages of railroad workers from the jurisdiction of bankruptcy judges, thereby evidencing an intent to have NLRA contracts treated in the same manner as any other executory contract. 11 U.S.C. §1167.* Obviously, both aspects of this argument are predicated upon Congressional silence. For that reason, and for several other reasons, both versions lack merit.

The 1978 revisions in the bankruptcy laws were made two years after the decisions in *Kevin Steel* and *REA Express*. Congress is presumed to be aware of judicial interpretations of statutes when it reenacts legislation. *Lorillard* v. *Pons*, 434 U.S. 575, 580-581 (1978). When Congress reenacted §365(a) it did not alter it in any substantial manner. Congressional promulgation of a provision without substantial alteration strongly supports an intent by Congress to approve of and adopt the existing judicial interpretations of that statute. *Cannon* v. *University of Chicago*, 411 U.S. 677, 696-698 (1979); *NLRB* v. *Gullett Gin Co.*, 340 U.S. 361, 366 (1951). More

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*11 U.S.C. §1167 of the Code (11 U.S.C. §205(n) of the superseded Bankruptcy Act) provides in relevant part that no judge shall change the wages or working conditions of railroad employees except in the manner prescribed in §156 of the Railway Labor Act.

importantly, judicial deference to labor contracts under §365(a) and its predecessor provision was never premised upon any particular language in the statute. Rather, it was grounded in the sound recognition of the unique nature and important role of labor contracts. *In re David Rosow, Inc.*, 9 B.R. at 192. Those same policy considerations still pertain, and none of the modifications made in reenacting §365(a) diminish or preclude the applicability of those considerations to the current statute. *Id.*

Nor is the exemption in §1167 for wages and working conditions for railway workers pertinent here. Preliminarily it should be noted that the Railway Labor Act was passed in 1933, the exemption in §1167 was enacted in 1934, the NLRA was created in 1935, and §8(d) of the NLRA was added in 1947. This legislative history hardly permits the inference that in enacting the railway workers' exemption in 1934 Congress deliberately intended to affect a statutory scheme which did not yet exist or a statutory provision which was enacted 15 years later. Note, *Bankruptcy and the Rejection of Collective Bargaining Agreements, supra* at 828. Moreover, the very courts which rejected the argument that the exemption in §1167 for railway workers should be applied to NLRA contracts are the same ones which established the special, rigorous test for labor contracts. *BRAC* v. *REA Express, supra; Shopmen's Local No. 455* v. *Kevin Steel, supra.*

Unlike this Union, the unions in those cases contended that NLRA contracts should be construed as within the §1167 exemption. While finding the arguments mustered by those unions appealing, the courts were ultimately unpersuaded. Thus, as in *REA Express* and *Kevin Steel,* the courts refused to completely immunize NLRA contracts from the purview of §365(a). However, and significantly, those same courts recognized the extraordinary nature of labor contracts and concluded that, though reviewable under §365(a), they should be treated with ex-

treme caution. Clearly the existence of §1167 does not and should not detract from the strict test established by the Second Circuit for evaluating NLRA contracts under §365(a).

Ineluctably, this Court is burdened with the task of defining the standard by which a labor contract should be rejected. Though the conflict between the circuits must now be left behind, their disagreement has at least forged the issue: should the rights of the workers be utterly destroyed simply to ease the recovery of a troubled company, or should those rights be preserved unless their sacrifice is absolutely necessary to the successful rehabilitation of the company and the preservation of the jobs themselves. The Draconian consequences of rejection must not be forgotten or belittled, for they include nothing less than wages, pensions, health insurance, seniority, arbitration rights, and unionism itself. No more fundamental rights exist in a free economy than those attached to the ability to secure and preserve a decent wage, a pension for retirement, and the medical needs of one's family. Surely these basic needs and rights should be preserved unless necessary for survival of the company and the preservation of the jobs. This Union asks no more, this nation's workers deserve no less.

CONCLUSION

For all of the foregoing reasons it is respectfully submitted that the judgment of the Court of Appeals should be affirmed in so far as it reverses the decision of the District Court, but that it should be reversed in so far as it delineates the role of the labor laws and the standard for rejection of a labor contract in a bankruptcy proceeding.

Respectfully submitted,

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